IN THE

# Supreme Court of the United States

OCTOBER TERM, 1945

No. 356

WINTER REALTY & CONSTRUCTION CO.,
*Petitioner,*

*against*

COMMISSIONER OF INTERNAL REVENUE,
*Respondent.*

**PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT AND BRIEF IN SUPPORT OF PETITION**

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August 15, 1945.

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| WINTER REALTY & CONSTRUCTION CO., *Petitioner,* *against* COMMISSIONER OF INTERNAL REVENUE, *Respondent.* | No. |

## PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

*To the Honorable, the Chief Justice and the Associate Justices of the Supreme Court of the United States:*

Your petitioner, Winter Realty & Construction Co., respectfully prays that a writ of certiorari issue to review an order, judgment and decree of the United States Circuit Court of Appeals for the Second Circuit, entered on May 23, 1945 (R. 115), affirming in part and reversing in part an order and decision of The Tax Court of the United States entered on September 9, 1943 (R. 52-54). A certified transcript of the record is furnished herewith in accordance with Rule 38, Par. 1, of the Rules of this Court.

The opinion of the Tax Court (R. 13-45) is reported at 2 T. C. 38. The opinion of the Circuit Court of Appeals (R. 105-114) is reported at 149 F. (2d) 567.

## STATEMENT

Prior to 1932, the City of New York took by condemnation proceedings certain property owned by the petitioner (R. 16) which had a tax basis of $136,564.83. During the years 1932, 1935 and 1936, the City paid to the petitioner the respective net amounts of $160,092.81,* $125,735.57 and $101,116.25, aggregating $386,944.63, as compensation (exclusive of interest) for the property taken (R. 17, 41). Gain upon such awards was accordingly realized as follows (R. 17):

| | |
|---|---|
| 1932 | $ 23,527.98 |
| 1935 | 125,735.57 |
| 1936 | 101,116.10** |

The first award was received on May 12, 1932, in the net amount of $160,092.81 (R. 17, 41). Prior to the end of 1932, the petitioner made an application for permission to establish a replacement fund which was received but apparently lost (R. 19, 36). After making several inquiries about the first application, the petitioner made a second application to establish a replacement fund in 1937 (R. 22, 36). Neither of such applications was ever acted on by the Commissioner of Internal Revenue (R. 36, 37).

In closing its books for the year 1932, the petitioner set up on the liability side of its ledger an account called

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*The actual net amount paid in 1932 was $160,292.81, but since the Commissioner's determination omitted a $200 item, the lower amount is used. Neither party makes any issue of this discrepancy.

**Although the correct amount of gain was $101,116.25, the Commissioner claimed a tax on only the lesser figure of $101,116.10.

"replacement fund" in the full amount of the net condemnation award received in 1932 (R. 19). At the time the petitioner filed its 1932 income tax return, it also stated in an accompanying letter that it had set up a figure in such return headed "replacement fund", and that it was the petitioner's intention "to replace same in property similar or related in service or use to the property so converted; or, in the acquisition of control of corporation owning such other property" (R. 20).

In 1935, the petitioner received an additional award in the net amount of $125,735.57, and thereupon increased the amount of its account captioned "replacement fund" by the amount of the net award plus assessments (R. 21). Similarly, the petitioner increased the amount of such account by the amount of the net award of $101,116.25 which it received in 1936, plus assessments (R. 17, 21).

The petitioner forthwith invested $190,735.57 of the awards in real estate mortgages which were marked "replacement fund" (R. 21, 70).

**The Statute**

The applicable statute is § 112(f) of the Revenue Acts of 1932, 1934 and 1936 (47 Stat. 169, 48 Stat. 860, and 49 Stat. 1648, respectively). The section is identical in all three Acts, and reads as follows:

> "(f) INVOLUNTARY CONVERSION.—If property (as a result of its destruction in whole or in part, theft or seizure, or an exercise of the power of requisition or condemnation, or the threat or imminence thereof) is compulsorily or involuntarily converted into property similar or related in service or use to the property so converted, or into money

> which is forthwith in good faith, under regulations prescribed by the Commissioner with the approval of the Secretary, expended in the acquisition of other property similar or related in service or use to the property so converted, or in the acquisition of control of a corporation owning such other property, or in the establishment of a replacement fund, no gain or loss shall be recognized. If any part of the money is not so expended, the gain, if any, shall be recognized, but in an amount not in excess of the money which is not so expended."

The Treasury Regulations promulgated pursuant to such section under the above Revenue Acts are set forth in the Appendix to this petition. They provide that the taxpayer "may obtain permission to establish a replacement fund in his accounts", and should "make application" therefor.

**The Commissioner's Determination**

The Commissioner determined that no part of the awards were expended forthwith in the acquisition of other property similar or related in service or use to the property condemned or in the establishment of a replacement fund (R. 16). He accordingly determined that the entire amount of the capital gain realized for each of the years 1932, 1935 and 1936 was taxable to the petitioner.

**The Decision of the Tax Court**

The Tax Court decided the case as if the petitioner had obtained "permission to establish a replacement fund" under the Treasury Regulations (R. 37). (The statute does not require such permission). The Tax Court held, however, (against the petitioner) that no replacement fund

was established, mainly upon the ground that a large part of the award money was invested in real estate mortgages, which would probably not be regarded as an ideal investment for the purpose of a replacement fund (R. 38). The petitioner appealed from that portion of the Tax Court's decision.

The Tax Court also found that the petitioner forthwith expended $96,830.19 of the award money "in the acquisition of other property similar or related in service or use to the property so converted", $45,713.94 being thus expended in 1932 and $51,116.25 in 1936 (R. 26). The Commissioner did not press an appeal from those findings.

The Tax Court further held (in favor of the petitioner) that, since the capital gain from the condemnation awards was realized in each of the years of the payment of the awards, namely, 1932, 1935 and 1936, the award received in each year should be traced to see what amount was expended in the acquisition of similar property and that amount was to be applied in determining the amount of gain realized in that year. It held against the Commissioner's contention that the three years should be treated as a unit for the purpose of computing that part of the realized gain which was taxable (R. 40, 41, 51). The Commissioner appealed from that portion of the Tax Court's decision.

**The Decision of the Circuit Court of Appeals**

Upon the petitioner's appeal, the Circuit Court of Appeals inferentially disapproved the main ground of the Tax Court's decision, namely, that real estate mortgages were not a proper investment for a replacement fund. The Court said that it might "assume that entries on the owner's

books, such as the taxpayer here carried, if supported by bank deposits, or mortgages, would be permissible" (R. 109).

The Circuit Court of Appeals held, however, that the replacement fund set up by the petitioner was not within the statute and the Treasury Regulations *solely* because the Commissioner of Internal Revenue had not given permission to establish the fund. The Court said that "the Commissioner's inaction, however negligent, was certainly not a performance of the condition, and the Commissioner could not be estopped." (R. 110)

Upon the Commissioner's appeal, the Circuit Court of Appeals held that the Tax Court was wrong in the rule of tax accounting which it had used in determining how the amount of the award expended in the purchase of similar property should be applied against the realized gain. In so doing, the Court not only reversed the Tax Court on the question of proper tax accounting, but overruled a previous decision of its own which supported the Tax Court's view (*Wilmore Steamship Co., Inc.* v. *Commissioner*, 78 F. (2d) 667).

## JURISDICTION

Jurisdiction of this Court is invoked under § 240(a) of the Judicial Code, as amended by the Act of February 13, 1925 (43 Stat. 938, 28 U. S. C. § 348(a)). The date of the order, judgment and decree of the Circuit Court of Appeals for the Second Circuit to be reviewed is May 23, 1945 (R. 115).

## QUESTIONS PRESENTED

Two administrative questions of importance are presented.

1. Where a statute provides that gain shall not be recognized where property is involuntarily converted into money which is "forthwith in good faith, under regulations prescribed by the Commissioner with the approval of the Secretary, * * * expended in the establishment of a replacement fund", and Treasury Regulations promulgated under such statutory provision provide that the taxpayer "may obtain permission to establish a replacement fund in his accounts" and in such a case "should make application to the Commissioner", may the Commissioner, by ignoring applications filed pursuant to the Regulations, prevent the taxpayer from establishing a replacement fund where such fund is otherwise properly established?

2. Where the Tax Court has decided a question of tax accounting, namely, that each taxable year should be considered separately under § 112(f) where three awards are received in three different years, rather than considering all such years as a unit, does a Circuit Court of Appeals have the power to reverse such a holding of the Tax Court under the rule of *Dobson* v. *Commissioner,* 320 U. S. 489?

**REASONS RELIED UPON FOR ALLOWANCE OF THE WRIT**

1. The Circuit Court of Appeals has decided an important question of Federal administrative law which has not been, but should be, settled by this Court, namely, whether a Federal administrative officer (who by his own regulation prescribes that a taxpayer should ask permission before the taxpayer may have a privilege given to him by the statute) may, by simply ignoring applications for such permission and not acting thereon, deprive the taxpayer of the privileges which the statute prescribes.

2. The Circuit Court of Appeals has decided a Federal question in a way probably in conflict with applicable decisions of this Court, particularly *Dobson* v. *Commissioner*, 320 U. S. 489, in that it has reversed a holding of the Tax Court upon a question of proper tax accounting.

WHEREFORE, your petitioner respectfully prays that a writ of certiorari be issued out of and under the seal of this Court, directed to the United States Circuit Court of Appeals for the Second Judicial Circuit, sitting at New York, New York, commanding said Court to certify and send up to this Court, on a date to be designated, a full and complete transcript of the record and of all proceedings in the Circuit Court of Appeals had in this case, to the end that this case may be reviewed and determined by this Court; that the order, judgment and decree of the Circuit Court of Appeals be reversed; and that your petitioner be granted such other and further relief as may seem proper.

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